In the Supreme Court of the United States

October Term 1941

No. .....

A. CRAWFORD GREENE, Guardian of the Estate of Alice H. Lester, an incompetent person,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Brief in Support of Petition for Writ of Certiorari

References to the opinions below are supplied in the petition (p. 4).

A statement of the case has been given in the petition (pp. 2-4) and to avoid duplication is not repeated.

SPECIFICATIONS OF ERROR

The errors intended to be urged are those specified in the accompanying petition and numbered 1 to 3, inclusive (p. 5), the same being assigned as error.

SUMMARY OF ARGUMENT

Review by writ of certiorari is sought herein because the Circuit Court of Appeals for the Ninth Circuit has refused to apply state law and has thereby reached the extraordinary conclusion, for which there is no precedent, that payments made in discharge of an obligation of support imposed by state law are taxable as gifts under the federal law. This conclusion has been reached both through failure to apply and misapplication of decisions of this Court defining the impact of state law in federal tax controversies. It is demonstrable that as to the pertinence of local law in matters of the kind here involved, five judges of the court below disagree with the two judges of said court who decided this case. This brief will seek to show that in refusing to apply the local law, the decision below is out of line with controlling authority. The points are developed as follows:

I.

A consideration of California law is essential—not "immaterial"—to the determination of this case.

II.

The orders of the California court enforcing and measuring the obligation of support should have been accepted by the court below.

III.

The decision of this Court in *U. S. v. Pelzer,* ..... U. S. ....., 85 L. Ed. (Adv. Ops.) 625, has been misapplied.

IV.

Two judges of the Circuit Court of Appeals for the Ninth Circuit decided this case on grounds in direct con-

flict with the expressed views of the remaining five judges of said court, and in conflict with applicable decisions of this Court.

ARGUMENT

I.

A CONSIDERATION OF CALIFORNIA LAW IS ESSENTIAL—NOT "IMMATERIAL"—TO THE DETERMINATION OF THIS CASE.

The Circuit Court of Appeals below said "it is immaterial what local statutes said, or local courts held" (R. Vol. I, 120).

The foundation of this application for review is that the Circuit Court of Appeals should have, but did not, apply California law and follow the determinations of the California court. In petitioner's view there can be no proper decision of this case without reference to California law. Notwithstanding the decision below, it is submitted, without fear of contradiction by respondent, that if local law creates an obligation of support, payments made in discharge of that obligation are not taxable as gifts under the Revenue Act of 1932. Otherwise the payment of alimony,[1] separate maintenance,[2] support of either spouse by the other,[3] support of children by parents,[4]

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[1] 47 American jurisdictions have statutes permitting the court to award alimony in absolute divorce cases. *Vernier, American Family Laws*, Vol. 2, p. 265.

[2] 36 states provide by statute for separate maintenance of the wife. *Vernier, American Family Laws*, Vol. 2, pp. 471-491.

[3] Many states provide by statute for the support of either spouse by the other. *Vernier, American Family Laws*, Vol. 3, pp. 108-111.

[4] All but one (Kansas) of the 51 American jurisdictions have statutes imposing civil liability on parents for support of children. See *Vernier, American Family Laws*, Vol. 4, pp. 56-92.

support of parents and other relatives by children,[5] and other obligations imposed by and enforced under state law are taxable as gifts. Congress plainly did not and could not intend the Gift Tax Act to be so inclusive, and nothing in Section 503 of the Act or elsewhere will justify that interpretation. Throughout this case respondent has virtually conceded that to the extent that the payments involved were in saisfaction of an obligation created by California law they are not taxable as gifts. It is accordingly necessary in the determination of this case to look at the California law and see whether the payments were obligatory. The court below refused to take this essential step.

So far as the California law is concerned there is no doubt that it imposes an obligation of support against the incompetent's estate in favor of her husband and daughters. California Civil Code Section 206 and California Probate Code Section 1502 (Appendix p. ii) are explicit and in terms of the stipulated facts of this case (R. Vol. I, 52-63) require the support and maintenance of the incompetent's husband and daughters from her estate.

> *Estate of Lynch*, 5 Coffey Probate Reports 279 (Cal. 1894),

held that these statutes created an obligation of support enforceable against the estate of an incompetent woman in favor of her adult son. There is no authority to the contrary. The Board of Tax Appeals held that there was

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[5] A civil obligation of children to support parents exists by statute in all but 11 American jurisdictions. *Vernier, American Family Laws*, Vol. 4, pp. 93-109.

an obligation under California law (R. Vol. I, 78, 80-81; 41 B.T.A. 515, 523), as did the dissenting opinion in the Circuit Court of Appeals (R. Vol. I, 121, 122). The majority opinion below simply refused to consider the question, holding that California law is "immaterial" (R. Vol. I, 112, 120). Petitioner was and is entitled to have his case decided in the light of the California law.

The only payments in question before the Circuit Court of Appeals were those for support and maintenance. It is stipulated that prior to 1937 the California probate court refused to order any payments to the husband and daughters except for maintenance and support (R. Vol. I, 52, 55, 56). During 1937 and under California Probate Code Section 1558 (Appendix pp. ii-iii), which was enacted in 1935, payments were ordered made to the daughters from surplus income of the incompetent's estate other than and in addition to the allowances for maintenance and support (R. Vol. I, 56, 57). The Board of Tax Appeals held such additional surplus income payments taxable as gifts (R. Vol. I, 78, 81-83; 41 B. T. A. 515, 523, 524) and petitioner has not appealed from that determination.

II.

THE ORDERS OF THE CALIFORNIA COURT ENFORCING AND MEASURING THE OBLIGATION OF SUPPORT SHOULD HAVE BEEN ACCEPTED BY THE COURT BELOW.

If it is clear, as petitioner contends and as determined by the Board of Tax Appeals and by the only judge of the Circuit Court of Appeals who did not disregard the question, that California law imposed an obligation of

support which was enforced by the California probate court administering the incompetent's estate, then that court's measure of the obligation is conclusive in this tax controversy.

Freuler v. Helvering, 291 U. S. 35;
Blair v. Commissioner, 300 U. S. 5,

and a host of cases in the Circuit Courts of Appeals and before the Board of Tax Appeals support this view. The orders were made by the court which has administered the incompetent's estate for more than thirty years and is thoroughly familiar with the situation of the incompetent, her children and her property. In each of those orders the probate court found that the payees were "members of the family" of the incompetent, "wholly dependent upon the estate of Alice H. Lester for maintenance and support and have no other means with which to defray living expenses", and that "it is necessary for the comfortable and suitable maintenance and support of the family of said Alice H. Lester, of which petitioner is a member," that the allowances be made (e. g., R. Vol. II, Exhibit 1-F—page 2 of order dated November 28, 1931). The orders for support and maintenance have become final judgments.

California Probate Code, Sections 1240, 1630;
California Code of Civil Procedure, Sections 963, 939.

The conclusion of the California court that the daughters were dependent on their mother's estate and that the allowances are necessary for their support, and its decrees

ordering the payments for support and maintenance, are final in this tax proceeding. In the language of

Blair v. Commissioner, 300 U. S. 5, at 10:

> "To derogate from the authority of that conclusion and of the decree it commanded, so far as the question is one of state law, would be wholly unwarranted in the exercise of federal jurisdiction."

The *Blair* and *Freuler* cases, and other cases in the Circuit Courts of Appeals and before the Board of Tax Appeals which follow the rule of those cases, were brushed aside in the majority opinion of the court below with the comment that

> "None of such cases involve the gift tax act and are, therefore, not in point." (R. Vol. I, 120)

Thus the rule which has been consistently applied in Income and Estate tax cases is held to be inapplicable to the Gift Tax Act, without any citation of authority and without any statement of reasons for this important conclusion. It is plain from the holding of this Court in the *Blair* case that the principle announced therein is one of the appropriate exercise of federal jurisdiction in the administration of federal tax laws and in no way turns upon the particular Revenue Act involved. There is neither reason nor authority for the conclusion that the principle referred to has no application to the Gift Tax Act.

III.

THE DECISION OF THIS COURT IN U. S. v. PELZER, ... U. S. ....., 85 L. ED. (ADV. OPS.) 625, HAS BEEN MISAPPLIED.

It appears that the Circuit Court of Appeals reached its conclusion that California law is "immaterial" in this case in reliance upon the decision of this Court in

United States v. Pelzer, ... U. S. ....., 85 L. Ed. (Adv. Ops.) 625.

The *Pelzer* case was decided March 3, 1941, after this case was argued and submitted to the Circuit Court of Appeals (R. Vol. I, 111), and although petitioner's petition for a rehearing in that court stressed the fact that he had not been heard on the applicability of the *Pelzer* case as controlling authority herein, said petition for rehearing was denied (R. Vol. I, 124). The *Pelzer* case involved Section 504 (b) of the Gift Tax Act, which provides that the first $5,000 of each gift (other than of future interests in property) made to any person by the donor is excluded in computing the tax. The taxpayer in that case contended that the term "future interests" should be defined by the law of the state where his gifts in trust were made. This Court held that there was no implication in the exclusion of gifts of "future interests" from the benefits given by said Section 504 (b) that state law should control the definition of "future interests". After quoting from the *Pelzer* case the majority opinion of the Circuit Court of Appeals refers to Section 503 of the Gift Tax Act, which provides that a transfer of property for less than full and adequate consideration

in money or money's worth shall be deemed a gift to the extent that the value of the property exceeds the value of the consideration, and concludes that the term "consideration" as used in said section is not to be defined by local law (R. Vol. I, 119, 120). Petitioner does not dispute that conclusion, but insists that it affords no basis for deciding this case, or for holding that payments made in discharge of an obligation imposed by local law are gifts. In the language of the dissenting opinion of Judge Stephens, the determination that *consideration* is not to be defined by local law "is not to say that a transfer in discharge of a legal obligation imposed by local law is a transfer without consideration under the taxing act" (R. Vol. I, 122).

The *Pelzer* case has been cited as controlling authority for a conclusion it in no way supports, viz.: that local law is immaterial herein and hence these payments, though made in discharge of a legal obligation imposed by local law, are taxable gifts. Petitioner submits that misapplication of the *Pelzer* case, particularly as it reaches a result in conflict with other decisions of this Court (*supra*, pp. 6-8, 18-19) is ground for review by certiorari herein. In

Helvering v. Fuller, 310 U. S. 69,

this Court granted certiorari "because of the asserted misapplication by the Circuit Court of Appeals of the rule" of a case decided by this Court (310 U. S. 71).

IV.

TWO JUDGES OF THE CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT DECIDED THIS CASE ON GROUNDS IN DIRECT CONFLICT WITH THE EXPRESSED VIEWS OF THE REMAINING FIVE JUDGES OF SAID COURT, AND IN CONFLICT WITH APPLICABLE DECISIONS OF THIS COURT.

The disagreement between the judges of the Circuit Court of Appeals for the Ninth Circuit as regards the crucial question in this case—whether local law applies in federal tax cases—presents an interesting situation which requires the attention of this Court. Consideration of the opinions of that court indicates that the two judges who decided this case are not applying local law, whereas the other five judges follow the decisions of this Court and readily apply the local law whenever the taxing statute either by express language or necessary implication makes its operation dependent upon local law. The following cases particularly demonstrate this conflict.

In

Bank of America v. Commissioner, 90 F (2d) 981,

the question was whether all or only half of the proceeds of insurance on decedent's life should be included in his estate for estate tax purposes. The insured and his wife resided in California and the insurance premiums had been paid from community funds. The executrix of decedent's estate claimed that under California community property law the wife was the owner of one-half the insurance proceeds and that accordingly only one-half thereof should be included in the decedent's estate. Judges

Haney and Garrecht said that "* * * whatever the local law may be we believe it to be immaterial * * *" (90 F (2d) 981 at 983), and held that the entire proceeds should be included in decedent's estate. Judge Wilbur dissented. There was no application to this Court for review.

In

Lang's Estate v. Commissioner, 97 F (2d) 867,

the question was identical with that involved in the *Bank of America* case, except that Washington community property law was relied upon by the taxpayer. Referring to the *Bank of America* case and the statement therein that local law is immaterial, Judge Denman, with Judges Mathews and Healy concurring, said (97 F (2d) at 869-870):

> "There was a dissent and this court was faced with the situation where the decision of two judges of the circuit made a precedent for the remaining five. The three judges sitting in this review did not agree with the decision in the Bank of America Case. Since no more than three judges may sit in the Circuit Court of Appeals, there is no method of hearing or rehearing by a larger number. Hence, rather than overrule the holding of the Bank of America Case, it was decided to present a certificate to the Supreme Court disclosing the conflict between the two groups of judges and asking that it be resolved by that tribunal.
>
> The Supreme Court responded by deciding that the Washington community law should be considered in determining the tax liability:
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> 'Occasion for the certificate did not arise from doubts relating to the meaning of the community property laws of Washington, but from uncertainty

> concerning the application of the 1926 Revenue Act to an estate under administration in that State. The court was perplexed by Bank of America v. Commissioner of Internal Revenue, 9 Cir., 90 F. 2d 981, 983, which affirmed that the operation of that Act is not dependent upon local law and "therefore, whatever the local law may be, we believe it to be immaterial." This statement is not accurate and conflicts with what we have said. Poe v. Seaborn, 282 U. S. 101, 111, 112, 51 S. Ct. 58, 59, 75 L. Ed. 239; Blair v. Com'r, 300 U. S. 5, 9, 10, 57 S. Ct. 330, 331, 332, 81 L. Ed. 465.' Lang v. Com'r, 58 S. Ct. 880, 882, 82 L. Ed. ....., May 16, 1938."

The *caveat* of this Court, quoted above, has been disregarded in the present case, for Judges Haney and Garrecht, with Judge Stephens dissenting, have now again said that local law is "immaterial" in a case where by necessary implication the operation of the Gift Tax Act is dependent upon state law. Moreover, these judges have now also said that because *Blair v. Commissioner*, 300 U. S. 5, did not involve the Gift Tax Act, it is not in point here (R. Vol. I, 120). But the *Blair* case did not involve the estate tax act either, yet in the above quotation from *Lang v. Commissioner*, 304 U. S. 264, an estate tax case, it was cited by this Court as controlling.

This conflict between these judges is further evidenced by the opinion in

Ingraham v. Commissioner, 119 F. (2d) 223,

decided just ten days prior to the present case. That was an income tax case in which Judges Denman, Mathews

and Stephens applied Connecticut law without hesitation or question to determine whether the taxpayer was under a continuing obligation to support his wife and children notwithstanding a Connecticut divorce and establishment of a trust providing for income payments to the wife. They held that under a Connecticut statute as generally construed the husband was under no continuing obligation to support his wife and, accordingly, that the trust income paid to her was not taxable to him except to the extent that it was used by her to discharge his continuing obligation to the children.

In the present case the payments taxed were admittedly for "support and maintenance" of members of the incompetent's family. Petitioner contends that they were not gifts because made in discharge of an obligation imposed by California law. The existence of that obligation must be determined by reference to California law. Unless all payments for support of wife, children and relatives are to be taxed as gifts under the Revenue Act of 1932, whether obligatory under state law or not, this case cannot properly be decided without reference to California law. Judges Haney and Garrecht have refused to consider California law.

In view of this conflict between the judges of the Circuit Court of Appeals for the Ninth Circuit, a litigant whose tax liability depends upon the applicability of state law may obtain one judgment if his case is assigned to the judges who hold that local law is "immaterial" and a different judgment if his cause is assigned to the other judges of that court.

In this instance the failure to apply state law resulted in a judgment that money paid to satisfy an obligation of support imposed by state law is taxable as a gift under federal law. If that judgment is valid, the most important single distinguishing feature of a gift—donative intention—has been obliterated for purposes of the Gift Tax Act and the payment of any debt enforced under state law may be taxable as a gift under federal law. This is a most important federal question. It has been decided without precedent by two judges of the Circuit Court of Appeals with whom five of their colleagues disagree as to the principles involved.

In *John Hancock Mutual Life Ins. Co. v. Bartels*, 308 U. S. 180, this Court said: "Because of conflict in the rulings of the Circuit Court of Appeals for the Fifth Circuit, due to the differing views of the judges composing the court in the case cited, and because of the importance of the question, we granted certiorari, * * *" (308 U. S. at 181). For the same reasons, and the others set forth herein, petitioner prays that certiorari be granted in this case.

Respectfully submitted,

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Of Counsel.

Dated: San Francisco, California, June 21, 1941.

APPENDIX FOLLOWS